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Omond, Thomas Stewart

The national debt: its origin and political significance.

THE NATIONAL DEBT: ITS ORIGIN AND POLITICAL SIGNIFICANCE.

THE

STANHOPE PRIZE ESSAY FOR 1870.

BY

T. S. OMOND,

EXHIBITIONER OF BALLIOL.

"Veniam pro laude peto."

OXFORD:

J. AND G. SHRIMPTON.

1870.

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The National Debt: its Origin and Political Significance.

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THE expenditure of a nation is necessarily greater in time of war than during peace. This temporary burden is naturally met by a temporary increase of taxation. But as this special pressure falls on the nation at the very time when its resources are least able to bear such a sudden strain, statesmen have conceived the idea of distributing the pressure over several years, by borrowing sums which are to be repaid gradually, when the return of peace has lessened the national expenditure, and at the same time increased its revenue. Thus, instead of providing beforehand for a rainy day, they adroitly contrive to enjoy the full fruits of provision during the season of storm, anticipating a period of sunshine when they shall justify their enjoyment. It is not two centuries since this policy was first adopted in England to any serious extent; yet already, thanks to the great facilities which this plan presents for meeting emergencies, and the large amount of capital lying ready for investment, the National Debt has swelled to a sum which cannot be discharged for years, perhaps for generations, and the interest on which, so long ago as 1827, formed no less than half of our yearly expenditure[a]. But, strange to say, and in spite of the adverse predictions of some of our most eminent political economists, the country has wholly refused to be swamped by this enormous burden; wealth and prosperity have increased in proportion to the increase of our debt; so that, finally, very general credence has been obtained for the paradoxical-seeming proposition that the National Debt, so far from being an encumbrance and a sign of approaching dissolution, is actually one of the chief sources of our national greatness.

The possibility of creating these enormous loans speaks volumes for the confidence reposed in Government. Before the Revolution of 1688, no such confidence existed, no such pecuniary transactions were possible. Insurrections were

[a] "Edinburgh Review," vol. xlvi. p. 397, (October, 1827).

easily stirred up, for they cost the country at large but little; and no one would lend money to the Red Rose, when next week the White might be on the throne. Nor was there the same necessity of borrowing. In those primitive times, the revenue derived from the Crown lands, together with the special payments due on certain occasions from feudal vassals, sufficed for the ordinary expenditure of royalty. The king was but one of the great lords; like them, he had his income, and, like them, his chief expense was the maintenance of his household. When the breaking out of war entailed on him unusual expenditure, it was provided for by a special and temporary addition to the Exchequer. The form which these supplies took was either a voluntary loan on the part of individuals, or a grant by Parliament of certain taxes, which were to be levied for that year only.

This inability of the Crown to levy taxes, without express Parliamentary authority, is one of the most remarkable features of all early European governments. The voluntary character of the "benevolences" contributed by private munificence is sufficiently established by the name, though Macaulay observes that our Plantagenet monarchs sometimes "begged in a tone not easily to be distinguished from that of command, and borrowed with small thought of repaying[b]." The sole power of taxing was always vested in a legislative assembly, known variously as Parliament, Cortes, Estates, &c. It is easy to prove that this was the case in England, however often ambitious monarchs may have assumed the right. The famous statute of Edward I.[c] laid down the principle clearly, and it is frequently appealed to in subsequent Acts, as in one of Charles I.[d], which begins: "Forasmuch as it is and hath been the ancient right of the subjects of this realm that no subsidy, custom, impost, or other charge whatsoever ought or may be laid or imposed upon any merchandise, exported or imported by subjects, denizens, or aliens, without common consent in Parliament." In the words of Blackstone, "it is the antient, indisputable privilege and right of the House of Commons, that all grants of subsidies or Parliamentary aids do begin in their house, and are first bestowed by them[e]." And many other passages might be adduced[f].

It is not, of course, meant that this privilege of Parlia-

[b] Macaulay's History, vol. i. p. 15.
[c] 34 Edw. I., cap. 4, headed "Statutum de Tallagio non Concedendo."
[d] 16 Car. I., cap. 8.
[e] Comm., bk. iv. cap. 1.
[f] It is in fact conceded by all writers, though Hume attributes its origin to the weakness of the Lancastrian sovereigns, (Hist., chap. xix. end).

ment was invariably respected. In truth, its infringement brought on the great battle between Crown and Commons, which culminated in the overthrow of the Stuarts. Still such was the law of the land; and there are numerous instances on record, where a too open want of regard for it excited resistance and rebellion[g]. And during the French wars, our kings found Parliament so ready with their supplies, that they never thought of looking elsewhere; hence what was already possessed of legal right assumed the yet more inviolable sanctity of custom.

As yet, however, these taxes were only temporary. The necessity for levying them permanently arose from the same cause which predisposed the people to their permanent contribution. As the feudal system declined, the military service which it demanded became distasteful to the smaller vassals—hence the necessity for a standing army—and a habit became general of commuting that service for money —hence the means of maintaining a standing army. In France, it was not long before this payment, which was known as the *Taille*, became annual instead of occasional, and was extended from landholders to tenants of houses. As the superior vassals continued to serve, while ecclesiastics had always been exempt, the tax fell exclusively on the commons[h]. It was the province of the "Estates," upon emergencies, to extend it for a time to the other two orders.

In England, fortunately, the necessity of a standing army was not felt until the example of our continental neighbours had opened our eyes to its danger. To neutralise the accession of power which the Crown received from the possession of an army, Parliament insisted that the taxes necessitated by that possession should be paid to them. This, though so far a change, was unquestionably the proper and constitutional developement of the old principle that taxes, sanctioned by Parliament, be paid to the Crown; and its final triumph secured the victory of mixed over absolute monarchy in England. Our sovereigns were well aware of the importance of this movement, and resisted it strenuously[i]. From the time of Elizabeth, when the defeat of the Spanish Armada left England free to turn its attention to home reforms, through well-nigh three generations the contest was carried on, "bequeathed from sire to son." The lead-

[g] E.g. Mead's Letters, vol. iii. p. 392: "On Monday the judges sat in Westminster Hall to persuade the people to pay subsidies; but there arose a great tumultuous shout amongst them, 'A parliament, a parliament, else no subsidies!'" This was in Charles the First's time, but the same feeling appears during the reigns of the most absolute monarchs.

[h] "France under Richelieu and Colbert," by J. H. Bridges, p. 78. The *Taille* became annual and permanent about the year A.D. 1445.

[i] De Lolme "On the Constitution of England," book i. chap. vi.

ing positions in that great campaign, from 1601 to 1688, are known to all. The limitation of Monopolies; the firm position which the weakness of James I. encouraged the Commons to take up; the famous Petition of Right; the yet more famous struggle against Ship-money; the interval from 1640 to 1660, when England was virtually ruled, first by an oligarchy, then by an absolute monarch; the return to the old Government, and renewal of the struggle between Crown and Commons; the French alliance, by which the last two Stuart kings avoided meeting Parliament; led up, at length, to the expulsion of the Stuarts, and the presentation of the Crown by Parliament to the Prince of Orange. Parliament had gained the victory, and remained unchallenged masters of the field. The right of taxation, the right of originating financial measures, was, from henceforth, theirs alone. Succeeding sovereigns, owing the sceptre virtually to their election, were little disposed to renew the struggle; and from that time there has never been any danger of the functions legally vested in the two Houses being over-ridden by exercise of the royal prerogative.

Parliament had gained the victory. But the resources of the country had been severely tried; and the war against the deposed monarch demanded fresh exertions. The customs' and excise duties were bringing in but half of what they had done before the Revolution: the land-tax had to be raised to four shillings in the pound[j]. All was inadequate to meet the extraordinary sums which Parliament voted for the maintenance of the army with which William was supporting the Confederacy. Nearly £4,000,000 had been assigned between army and navy; the largest war-vote then on record. Montague and Godolphin exhausted every expedient in the endeavour to defray these sums from the yearly revenue, but the country was still too unsettled to stand a heavier taxation. At length they resolved to have recourse to an expedient which had been long in use on the Continent, and was not wholly unfamiliar to English statesmen. So early as A.D. 1334, the Government of Florence had set the example of borrowing money in time of distress, and repaying it when their troubles had ceased. "This Government," says Blackstone, "then owed about £60,000 sterling; and, being unable to pay it, formed the principal into an aggregate sum, called, metaphorically, a *mount*, or *bank*, the shares whereof were transferable, like our stock[k]." The Banks of St. George at Genoa, of Venice,

[j] "An Essay upon Ways and Means," (Francis Davenant?) pp. 35, 36, giving comparative tables.

[k] Commentaries, bk. i. chap. 8.

and of Amsterdam, were instances of the same practice[l]. The Popes had subsequently adopted a similar financial method in their sale of offices, receiving a net sum, and paying an annual salary[m]. In France it had lately been introduced, against the earnest advice of Colbert[n]; and several European nations had adopted it. So long ago as the time of Henry IV. the English Government had been compelled to anticipate its resources[o]; and James II. had left behind him a debt of between six and seven hundred thousand pounds[p]. But this was a mere casual encumbrance, not reduced to any regular form. The financiers of 1693 determined to follow out the precedent systematically.

The expediency of this step has been often questioned by writers who regarded the National Debt as an unmixed evil and danger. The original scheme was ascribed to men of revolutionary character. Old-fashioned Tories used to credit Bishop Burnet with its invention; Swift and Bolingbroke inveighed against it as a bribe to the moneyed interest; while the Jacobites did not fail to assert that William III. had purposely created our pecuniary difficulties. But this is the injustice of men who judge by results. There was no choice left at the time. The Jacobites, watching eagerly for every means of arousing national discontent, would have made good use of the opportunity which any increase of an already burdensome taxation could not have failed to afford[q]. The country had to be humoured and kept quiet; while at the same time the expenditure had increased fourfold in the course of a few years. Not only was there ample precedent in English history, and encouragement in Continental, for the measure, but the facilities for carrying it out arose simultaneously with the necessity. Individuals were wealthy, though the country was in need. While the landed interest was sorely burdened, and the people taxed as high as they would bear, money was actually lying idle for want of a safe investment, or being squandered on chimerical projects. Under such circumstances, to have neglected the opportunity would not only have been foolish, it would have been suicidal. So far from the creation of our National Debt being hazardous and reprehensible, it was the imperative duty of William's ministers to create it.

[l] Hallam's Middle Ages, chap. ix. part ii.; Macaulay's History, chap. xx. p. 55.

[m] Ranke's History of the Popes, i. 4, 2.

[n] Bridges, p. 86.

[o] Hume, vol. iii. chap. xxi., end.

[p] Hamilton "On the National Debt," 3rd edition, p. 92. This debt, known as the "Banker's Debt," was incorporated with the others in 1716. Ibid., p. 66.

[q] The most absolute monarchs are cautious how they irritate their subjects by increase of taxation. Even the Sultans seldom levy taxes. Hume, "Essay on Taxes;" Brougham, "Political Philosophy," part i. chap. iii.

It is not meant, however, to prejudge the question as to the advantage or disadvantage of possessing a National Debt. The schemes first proposed were entirely temporary: the burden was merely distributed over many years instead of being met at once. For a long time it was looked that the loans contracted should be discharged on the return of more prosperous years. These expectations always proved illusory: the question remains whether it had not been wiser to have made special efforts to obliterate the debt, instead of plunging deeper and deeper, more and more recklessly, into the gulf, perpetuating old obligations and contracting new, till the total swelled to a sum whose interest cost the nation every year as much as a war would have done.

The first beginnings, however, were on a sufficiently moderate scale. A loan of one million was voted, and an unpretending-looking statute enacted that certain duties on ale and beer were to be set aside for its repayment[r]. The form of this first loan was a *tontine*; an arrangement not so popular in England as elsewhere. Each subscriber of £100 was to name a life. The interest, which was fixed at 10 per cent., was to be paid to the nominee from the said tax on beer. As the annuitants died off, their annuities were to be divided among the survivors, till these were reduced to seven, after which each as it fell in went to the public. The last nominee died in 1783[s]. Though the interest appears high to us, it must be remembered that the risks were not small. As confidence spread, the rate of interest was lowered, till Mr. Pelham's measure (1749) reduced it to its present denomination.

Encouraged by the success of this measure, Government in the following year turned its attention to a scheme which had been lying before them for three years, having been submitted by William Paterson, who afterwards attained such an evil notoriety by his South Sea Scheme. This was a proposal to constitute a Bank of England, on the same footing as those of Genoa and Amsterdam[t]. The time was ripe for such a project. The vast increase of money above referred to had created our system of private banking. General curiosity had been excited on the subject, and on the expediency of a National Bank. The year just gone by had seen an absurd prospectus by Dr. Hugh Chamberlayne laid before the House. Paterson's plan, besides having the advantage of priority, was modest and sensible where Chamberlayne's was arrogant and absurd. It was accordingly taken up by Montague, and by Michael Godfrey an

[r] 4 G. & M., cap. 3. [s] Macaulay, *in loco*; Hamilton, note 12.
[t] Macaulay, ch. xx. p. 54; Francis' History of the Bank of England, ch. iii.

eminent merchant, who was to secure the support of the City. After many difficulties, which are graphically described by Macaulay, the Bank of England was constituted [u]. £1,200,000 was to be advanced to Government, at the then low rate of 8 per cent., on the understanding that the creditors should not have the power of demanding back their money, while Government reserved the right of paying them off. The sum was contributed in ten days.

The political significance of this measure can hardly be overrated. Not only was it the first permanent National Debt contracted by an English Government, but it created an institution without which our present system of transference of stock would hardly have been possible, to which the entire management of the Debt was before long handed over, and whose influence ever works powerfully on the side of peace and order. Well-founded doubts were expressed of the power which the possession of the Bank might give the Crown [x]. This difficulty was obviated by a clause providing that the Bank should not advance money to the Crown without Parliamentary sanction. But it shews the confidence Parliament had in its own powers, the advance since the old Plantagenet and Tudor days, when they were content to rest on one clause that whole power of the purse, which seemed the only sufficient check on Royal encroachments, and whose spell had borne them in safety through the long and just-ended struggle with the Stuarts. Nobly has this confidence been borne out by experience. The Bank has indeed proved, as was expected, one of the principal props of the throne; had its institution taken place earlier in our history, it might have seriously interfered with our constitutional progress; but Montague and his friends were right in believing that for the future that danger was past, that not even another revolution could shake the hold which Parliament had on the reins of power, or endanger the foundations of public credit.

Yet the infancy of the Bank was no peaceful one; had the offspring of Montague's sagacity been of sicklier constitution, it must have perished in the cradle. The very next year brought to a climax the distress produced by a rapid deterioration of the coinage. The Re-coinage Bill of 1695 [y], carefully framed as it was, could not fail to produce a scarcity of money. That juncture was chosen by the enemies of the Bank for a general onslaught. The Bank could not meet their demands, and had to offer 15 per cent., endorsing their notes with a promise to pay the re-

[u] 5 and 6 G. & M., cap. 20, (see section 20).

[x] Cf. p. 22, infra.

[y] 7 and 8 G. III., cap. 1.

mainder when the new money should come out. Public credit seemed ruined[z]. But English love of fair-play led the nation to side with the Bank, and its promissory notes passed current. This was but one instance of the fine feeling displayed during that terrible crisis. For the danger was but begun. The fearful scarcity of money was prolonged by a general hoarding of the new coinage, people imagining that Parliament would be compelled to raise its value. William, from Holland, wrote urgent appeals for money to pay his soldiers. To add to the general confusion, an attempt on the part of the Opposition to found a Land Bank, as a rival to the Bank of England, broke down utterly. But that high spirit in time of danger carried England through this, as through many another crisis before that of 1862. All classes were like brothers. The rich lived on credit; the poor helped one another. Creditors forbore to press their claims; the soldiery were supported by the gentry, farmers, and shopkeepers. The shareholders of the Bank of England, despite the seeming failure of their enterprise, advanced £200,000 for the army in Flanders. Finally, Parliament declared that the value of the coin should on no account be raised. The effect of this true statesmanship was magical. The hoarded money poured into circulation at once: credit rose with a rebound that carried everything before it: and the National Bank and the principle of National loans received an impetus, and a lasting one, proportioned to their recent temporary stagnation.

Montague was not slow to take advantage of the reaction. Since the establishment of the first loan in 1693, another million had been raised by anticipation, the security this time being a fund formed by some new duties on salt[a], &c. and the form being changed from a tontine to a lottery. In 1696, in order to meet a deficit of five millions, both these taxes were continued, new ones imposed, the old loans were renewed, the practice of issuing Exchequer-bills, which had been introduced during the crisis of the preceding year, was continued, and all the taxes already mortgaged being thrown into one, greater confidence ensued. The National Debt was fairly set agoing, and its progress now was rapid, and in an ever-accelerating ratio. The land-tax was reduced, and not even the fall of Montague could breed distrust in the policy which he had inaugurated. It was not long before taxes, which had to be continually renewed, were made permanent.

The chief events in the progress of the National Debt

[z] A similar state of affairs will still be in the memory of some, lasting from 1797 to 1819.

[a] 5 and 6 G. & M., cap. 7.

down to the year 1715 need but be enumerated [b]. Everything seemed prosperous, taxes were reduced, and the public debts as yet trifling. At the peace of Ryswick, in 1697, the whole debt scarcely reached 21½ millions; at that of Utrecht, in 1713, it had not much more than doubled itself. Taking into account the unsettled state of the country, and the frequent wars in which it was involved, the increase was not excessive, and a few years of peace should have sufficed to reduce it considerably. The chief points of interest during this period are the various items of which the Debt is composed. The first loan was on life-annuities, but these were gradually converted into what were termed "long annuities" of ninety-six years' duration. Then there were annuities for a short time, generally sixteen years; and annuities on two, or even three lives. Besides these, there are the loans from the Bank of England and the East India Company, and a vast number of minor loans upon particular taxes, duties on excise, stamps, wines, tonnage and poundage, and the like. Exchequer-bills, too, as already mentioned, were issued by Montague; a practice greatly developed under subsequent administrations [c]. Towards the close of this period, moreover, and during the reign of Anne, the South Sea Company was established. Finally, when the long continuance of the "War of the Succession" had produced some tightness in the money-market, recourse was had to lotteries.

After the treaty of Utrecht, and during the peaceful reign of George I., a somewhat different policy was adopted. Instead of mortgaging the future produce of taxes, Government offered perpetual annuities, providing funds for the interest alone; an example since generally followed, though strongly reprobated by Adam Smith [d]. The multitudinous loans and taxes of preceding reigns were merged in two great funds, known as the *Aggregate* and the *General* funds, the surplus of one tax thus compensating for the deficit of another. The rate of interest, which had fallen during Queen Anne's reign from 8 to 6 per cent., was farther reduced to 5, and finally to 4. And the aggregate produce

[b] It is not proposed to introduce elaborate tables, which could only be copied from preceding writers, but merely to give a slight summary of the progress of our Debt. For details, see especially Hamilton's "Enquiry concerning the National Debt." References to particular passages there and elsewhere will occasionally be given. Round numbers have also been given, unless where special accuracy was necessary.

[c] Little notice has been taken in this Essay of the various unfunded debts incurred from time to time by Government. Their details are perpetually shifting, nor from their nature can they form a very serious item in the National Debt.

[d] "Wealth of Nations," book v. chap. iii. (M'Culloch's edition, 1846, p. 415).

of the general funds being in excess of the charges on them, the surplus was formed by Sir Robert Walpole into a "Sinking Fund," devoted to the discharge of the National Debt.

From this date the historian of the National Debt finds his task complicated by a succession of contemporary pamphlets, whose views are not always in accordance with what we have learned to think the indisputable deductions of political economy. The nation, restored to peace and leisure, began to turn its attention to this anomalous growth of some thirty years, and to ask how the Debtor was to meet his obligations. Wild ideas of reducing the burden by the iniquitous measure of taxing the funds are referred to by Harley, Earl of Oxford, in his "Essay upon Public Credit," (1710), and by the anonymous author of a "Letter upon the Inviolable Nature of Public Securities," (1717) [e]. But Walpole's scheme was the first systematic attempt at reduction, and it was naturally suggested by the adoption of perpetual funding in lieu of temporary mortgages. Into the merits of this scheme examination will be made hereafter; meantime we are content to trace its history.

The essence of the Sinking Fund was that it should never be even temporarily encroached on. At first this idea was honestly carried out: but it was not long before it came to an alternative between raising the land-tax and borrowing half-a-million from the fund. The decision was naturally for the latter, and the precedent was too tempting not to be followed. It seems, however, to be established that some reduction was effected by means of the Fund during the first ten years of its existence. This point, which formed the subject of a sharp discussion in the House of Commons between Sir Nathaniel Gould and Pulteney, supposed authors of rival pamphlets on the subject [f], is proved by a Memorandum which was presented by the House of Commons to George II., in 1728. The repeated encroachments on it, at any rate, soon rendered it useless, and justify Hamilton's observation that it did little in time of peace, and nothing in time of war, to the discharge of the National Debt [g].

The reign of George I. is thus remarkable as the beginning of the present state of affairs. The Sinking Fund, indeed, has long since vanished; but the convenient system of transference of stock, created when the Bank of England

[e] These, along with other scarce and interesting tracts on the subject of the National Debt, have been reprinted by Lord Overstone (1857), in a presentation volume, copies of which were presented to the chief libraries in the kingdom.

[f] "An Essay on the Public Debts of this Kingdom," 1726, (Sir N. G. ?); "State of the National Debt as it stood December 24, 1716," 1727 (Pulteney ?); "A Defence of an Essay on the Public Debts," 1727, (Sir N. G. ?).

[g] "Enquiry," p. 140.

assumed the management of the general funds, is still flourishing among us. Hitherto, we have had little fault to find with the management of the Debt; but we have now to survey more equivocal transactions, and to deplore a rush into headlong extravagance.

At the Accession of George II., in 1727, the Debt stood at a little over 52 millions. Thirty-six years after, at the conclusion of the Seven Years' War, it had risen above 138½. After twelve years of peace, during which 10 millions had been paid off, the American War broke out; and the eleven years of its continuance raised the Debt to 250 millions. The half-dozen years of peace which ensued, scarcely lowered this sum by as many millions: the French War followed with its two-and-twenty years of national peril and disaster: and when at length we emerged from that terrible and protracted trial, the Debt had reached the appalling total of 850 millions. When it is added that the slight reductions mentioned as occurring during this period were effected, not by virtue of a Sinking Fund, not from a surplus of revenue, but only by changing stock into life-annuities, it will be seen that during less than a century the nation, advancing *uninterruptedly* on its hazardous path, actually converted, in round numbers, a debt of 50 millions into a debt of 850.

It will readily be imagined that this prodigious burden would not have been laid on themselves by a people who really believed it to be a burden. It is to the theories of mistaken enthusiasts, who deluded the nation into believing it would prove no burden at all, but a vast assistance, that this haste to be in debt was due. During the reign of George II., indeed, but little novel was broached. The most noticeable points are the fluctuation of credit during the rebellion of 1745, and Pelham's reduction of interest in 1749; the latter a measure proposed by Sir John Barnard in 1737[h], but opposed by Walpole, and now carried amid general satisfaction. But there were no signs of an appreciation of the duty of curbing the natural tendency to extravagance. Philosophers began to be alarmed; Hume and Adam Smith painted our situation in the blackest colours, Hume declaring that there were but two alternatives, bankruptcy or repudiation—"either the nation must destroy

[h] See Sir John Barnard's pamphlet, "Considerations on the Proposal for Reducing the Interest on the National Debt," written in 1750, to explain Pelham's project. One sentence may be quoted to shew what, at that time, economy might have done: "If 1 per cent. were saved upon the Debt, and applied to the payment of the Debts, together with the growing savings, it would, without any other aid, pay off the whole redeemable Debt of the Nation in fifty-three years," (p. 29).

public credit, or public credit will destroy the nation[i]"—and Smith advocating the extension of our taxes to the Colonies as the only possible escape[k]. The nation shewed symptoms of uneasiness: an extensively read pamphlet, supposed to proceed from the pen of Lord Elibanke, did not hesitate openly to advocate repudiation[l]. People were ready to grasp at any means which promised extrication: their minds were in that state when they may be seized and carried captive by any quackery. Such an opportunity was not likely to be lost. The hour was come: the man was not wanting.

The Sinking Fund of 1716 did not depend for its efficacy on compound interest. The virtues of that species of arithmetic were first broached by Gould, whose pamphlet abovementioned has tables and statements shewing, among other things, that one million sterling, accumulated at 4 per cent. compound interest, would amount in 105 years to 1,575 millions. But it was reserved for Dr. Richard Price, in 1774, to win the ears of the nation by an eloquent restatement of Gould's views, and persuade them that they might double and quadruple their debt with impunity, provided they set aside annually a trifling sum for the Sinking Fund. Without pausing at present to consider the meaning or foundation of this statement, let us note the effect of it on the country. It was as if to a man entangled among frightful precipices, stumbling over jagged rocks, and shrinking back from treacherous crevasses, seeing no exit, and ready to give up in despair, a way was suddenly opened, a smooth path of flowers and meadow-grass, which led him without toil or danger to the peaceful valleys again. It was as if to a drowning man, clutching convulsively at any straw that floated by, an arm was suddenly extended, to lift him into a securely-built vessel. Little wonder if Pitt embraced the scheme with avidity, establishing, in 1786, his Sinking Fund on the ruins of that of Walpole: little wonder if the nation, released from its dismal forebodings, and taught to believe that the contraction of debt might be harmlessly carried to any extent, placed no check on its ministers, and welcomed any reasoning which lightened the taxes under which they were groaning. Down to the end of the French War this state of affairs lasted. Pitt's plans were variously modified, being altered in 1798 and in 1802, and finally discarded for rival plans built on the same hypothesis. Lord Henry Petty, for one year (1807), introduced a more complex edition of

[i] "Essay on Public Credit."
[k] "Wealth of Nations," closing pages.
[l] "Essays, I. On the Public Debt. II. On Paper-Money, Banking, &c. III. On Frugality," (1755).

the old scheme, and Vansittart attempted another reform in 1813; but all were mere modifications of Price's views. Nor must it be denied that some good resulted from the general credulity. The nation could scarcely have borne up as it did, but for some such artificial stimulus. The popular mind is prone to extremes: if they had not put faith in Price, they would probably have listened to Hume and Smith. And the actual loss which the Sinking Fund entailed on the country during the war with France (1794—1816) was, after all, but a drop in the bucket, being estimated by McCulloch at £557,857 per annum [m]. But these considerations cannot blind our eyes to the extreme carelessness of the financiers of that time, a spirit common to government and people, and created by the childish confidence reposed in what an anonymous writer calls "the operose jugglery of sinking funds." It is not so much that during that war half-a-million was squandered annually, or that, including that annual loss, some *fifty-two millions* were literally sacrificed for nothing [n]; but it is the thoughtless profusion, the utter disregard of economy, the consequent oppressive taxes—it is the reckless deductions for cash payment, the multitudinous *bonuses*, the constant habit of funding by increase of capital —it is practices like these, continued from the preceding war, and carried still further in this, which drive us to stigmatize the Sinking Fund system as a nurse of extravagance and carelessness, and to ascribe to its operation an infinitely larger proportion of our National Debt than the above-cited figures would lead us to suppose.

There had not been wanting attempts to break the spell of security which had been thrown over the nation, such as the anonymous "Considerations on the Annual Million Bill," published in 1787. But these attempts were ineffectual, until the publication of Professor Hamilton's Enquiry, which first opened people's eyes to the delusive nature of the system in which they had put their trust. By the time this consummation was reached, however, a change had come over public opinion. They saw their pet illusion melt into air; they saw the naked face of their extravagance, and owned their folly; but they saw also that the dismal prognostications of earlier writers had not been fulfilled. 80 millions had been spoken of as a frightful burden: when it reached 140, Hume had pronounced the case desperate;

[m] "Taxation and Funding," p. 459 (first edition). Be it remembered, however, that this annual outlay would have paid the interest on a loan of some 18½ millions at 3 per cent., on the system then in vogue, and that this estimate leaves out of account the Commissioners expenses, which were about £60,000 per annum.

[n] Ibid., p. 425.

but here they were paying the interest of 850 millions, and thriving in spite of their blinded prodigality. Granting they had been deceived as to the means of paying it off, what need was there of paying it off at all? Were we any the worse for it? Nay, was it not a positive good? In this comfortable persuasion we have remained for the last fifty years, growing in wealth, and reducing our taxes. Owning theoretically that the Debt is somewhat large, we do not fear any real danger from its bulk. What little has been done in the way of reduction has been done by honest devotion of surplus thereto. The Sinking Fund has been quietly given up, though at times Government has shewn some hankering after its old love[o]. There has also been a large amount of stock converted into terminable annuities, of which latter Government seems more fond than political economists are. But, for the most part, we take little heed of these things, unless when some enthusiastic *doctrinaire* mounts the National Debt as his hobby, or some public-spirited individual favours the Chancellor of the Exchequer with his contribution towards its discharge. The Debt has been reduced by about 100 millions, and the interest on it continues to absorb above a third of our revenue. When there is a surplus, we devote one-fourth of it to the reduction of the Debt[p]; but even this trifling sum (last year it amounted to £63,000 odd) we rather grudge. Any attempt to obtain more energetic dealing on the subject is good-humouredly turned aside by the Chancellor of the Exchequer[q]; and with this state of *laissez faire* the nation seems well content.

We have thus traced the history of the National Debt, and have observed how, after a period of anxious fear, and a period of sanguine hope, the country has sunk into a state of almost complete indifference on the subject. It is a somewhat singular phenomenon, and one is led to ask if it is natural. Is it fit that we should sit down contentedly under such a burden? Or, indeed, is it a burden at all? An answer to these questions will occupy the second part of this essay.

When a country is called on to make some special exertion, as in the case of a war, there are four ways in which the burden may be supported. First, the State may have amassed a treasure, which is now produced. Second, the taxation may be raised to an amount sufficient, year by year, to meet the year's expenses. Third, the State may borrow a sufficient sum to meet these expenses, and assign

[o] 18 and 19 Vict., cap. 18; cf. p. 32, note, infra. [p] By Act 29 and 30 Vict., cap. 39, act 16. [q] See Mr. Lowe's Budget-Speech, April 11, 1870.

certain taxes for the payment of interest, leaving the burden of repayment to some more favourable season. Or, fourth, the last-mentioned plan may be adopted, with an addition; sufficient taxes may be raised each year to leave a surplus after paying the interest, and this surplus be left to accumulate at compound interest until it reaches a sum sufficient to pay back the capital borrowed.

Of these, the first or antique plan has long been discarded. Its injurious effects, in withdrawing capital from circulation, are universally acknowledged. And the fourth, or "Sinking Fund" system, will be discussed in detail in the third section of this essay: besides that it is a modification of the preceding plan. The question, then, lies between meeting the expenditure by taxation, and meeting it by some system of borrowing. Which of these methods is it best for a nation to adopt?

The system of pure taxation has many obvious advantages, and is unreservedly recommended by Ricardo[r]. It is manifest that a wholesome check is thus supplied to undue haste in entering on a war, and extravagant expenditure during its prosecution. The burden is fairly laid on the nation, without concealment or disguise. Individuals are thus stimulated to exertion and economy during war, and are inspired with a salutary love of peace. Once the struggle is over, the nation is free again, instead of being burdened for many years, perhaps for ever, with debts contracted during its continuance.

Accordingly, most people are agreed that, whenever it is by any means feasible, this system ought unquestionably to be adopted. But, with all deference to the eminent writers who have held a different opinion, it does seem that such a course is not always possible. Theoretically, at least, there is a limit past which taxation cannot go, and therefore, theoretically at least, loans may at times be necessary. Moreover, as practical men, we are concerned, not only with the ideal of state management, but with the possibility under existing circumstances of a near approach to that ideal. Now our nation is burdened with a large annual sum due as interest on old loans, and this must be taken into account. It has repeatedly been determined by our Government in time of war, that, while the taxation was sufficient to meet the current expenses, it was inexpedient to raise it so as to defray also the interest of the old loans. This was the case during the last ten years of the French War[s]; and, costly as that struggle was, the expenses of warfare are increasing enormously. At the commencement of the

[r] "Essay on Funding System," Works (ed. M^cCulloch), p. 539.
[s] Hamilton's "Enquiry," p. 42.

Crimean War, Government announced its intention of meeting the expenses by taxation. During the first year, 14½ millions were thus raised, over and above the ordinary revenue: but this sum was found insufficient by half, and a loan of 16 millions had to be called for[t]. Even the late Abyssinian War, which cost less than 9 millions, has taken more than two years to defray[u]. It thus appears that, burdened as we are by old loans, it may be impossible by any exertion to raise our taxes to such a height as will meet the expenses of some given year.

A little reflection will shew us that there must be a limit to the extent of taxation a country can sustain. Enough must of course be left to supply the necessaries of life. But long ere we begin to trench on these, the drooping state of the country will shew that the mark has been overshot. Excessive taxation results in an immediate pressure on the poorer members of the community, and an ultimate pressure on employers, and capitalists generally. By no means can we prevent the burden from falling, in the long run, solely on employers[x]. Direct taxes (to use M^cCulloch's enumeration) may be on rent, profit, property and income, or wages. In each of the first three cases, the rich are evidently those affected. When taxes are levied on wages, or when they are levied indirectly, though the burden may fall at first on the poor, if it do not depress industry altogether, it will before long be shifted on to the shoulders of the employers. For the rate of wages is determined by shifting circumstances, and is variable: a rise in the price of provisions necessitates, in course of time, a corresponding increase of wages. Thus the employer eventually must defray both a tax on wages, and a tax on articles of consumption.

But, it will be said, is not this the very thing that justifies our increasing taxation indefinitely, since the burden, though it may cause temporary distress among the poor, falls ultimately on those who are best able to bear it? The answer must be, Capital will not bear taxing beyond a certain amount. The criterion of a country's wealth is the amount of capital it *employs*. But the power to increase capital depends on the rate of profit: these rise and fall together. A serious decline in the rate of profit is thus one of the heaviest calamities that can befall a country. The demand for labour is contracted. Capital is driven abroad. It has more than once happened in this country, when

[t] Supplement to Ricardo's Article, by his son, *Enc. Brit.*, 8th ed., vol. x. p. 342.

[u] And this, though the revenue was larger than it has been since 1815.

[x] For a fuller exposition of our line of argument, see "Edinburgh Review," vol. xlvi. p. 390.

too heavy taxation has produced a rise of wages, a rise in the price of food, and a corresponding fall of profit, that capitalists began to find it more remunerative to send their money abroad than to employ it in their own country. There is therefore a limit to the fall of profit which men will put up with rather than withdraw their capital from circulation; and consequently there is a limit to the imposition of taxes.

Seeing, then, that the safe rule of paying each year's expenses from the yearly taxes cannot always be complied with, it behoves us to enquire into the practical working of that system of loans which is in such cases our only resource. The Funding System possesses several striking advantages. It enables the nation to put forth its full resources on short notice. It relieves the country from excessive taxation, by distributing the burden over many years. Many, to whom a sudden payment of £1,000 would be impossible, have no difficulty in paying £50 annually[y]. It also creates a new trade, supplies a new outlet to the commercial spirit. It supplies a safe investment for those more anxious about security than profit. And it provides a very convenient substitute for ready money, since Government stock passes as freely as gold.

On the other hand, several drawbacks must be set against these advantages[z]. The ease with which loans are incurred is apt to make Governments careless and prodigal. To such a pitch has this extravagance sometimes mounted, that the very interest of the Debt has become a heavy burden. It tends to create a set of men who contribute nothing to the national industry, and, though this has been sometimes spoken of as a beneficial stimulus to the country, it seems a very dubious policy to feed a number of drones for the sake of getting more work out of their industrious brethren[a]. In order to maintain a safe investment for the few, it saddles the many with a perpetual burden, whereas it would be perfectly possible to furnish an equally safe investment with-

[y] It is argued by Ricardo that it would be just as easy for the individual to borrow as for the Government. But Government can borrow on far easier terms, as it offers infinitely better security. And few will be disposed to allow that the consequences of borrowing are as hurtful to a Government as to an individual.

[z] Many of the objections urged against the Funding System are of the most puerile nature. Among those enumerated by Hume, in his "Essay on Public Credit," are the following: "It tends to centralize men in London; it is a kind of paper-credit, deteriorating the value of gold and silver, and so raising the price of labour and provisions; it makes us, as it were, tributary to the foreigners who possess our stock."

[a] Stockjobbing, however, in spite of Lord Elibanke (see his "Essays on the Public Debt," p. 9), existed before the establishment of the Funding System, and would survive its discontinuance.

out any such burden at all[b]. Similarly, a less costly means of supplying a substitute for cash might be easily devised.

Opinions will always differ as to the weight to be attached to these considerations, and it would be easy to expatiate on each of them. But the real point at issue, when, in a period of distress, the question is raised as to the propriety of borrowing, is none the less very simple. Men ask, what objection is there of sufficient weight to counterbalance the present ease it affords? The great advantage of the measure is apparent; they see that it will save them from excessive taxation, and enable them to provide the requisite funds in the easiest possible way. Of the other advantages of the system they take little or no account: nor do they see much chance of serious evil accruing from its adoption. The opponents of the Funding System, well knowing its insidious nature, have yet no stronger argument to bring against its present adoption than the very intangible one that it fosters extravagance, and selfishly devolves our burdens on posterity. The logic of the latter assertion is perhaps not unimpeachable[c]: and neither is likely to have much weight at such a juncture. Against the possible disadvantages of borrowing men set the certain and serious evils of excessive taxation; and we cannot wonder if they decide in favour of borrowing. The common sense of the many in such a case judges rightly; there are times, such as the crisis that followed the Revolution of 1688, when it becomes the duty of a nation to avoid worse evils by the contraction of loans. No one would blame a land-owner who borrowed at 5 per cent., and laid out the money on improvements which brought him in 8 or 10. The case is the same with a nation.

Granting, therefore, the occasional necessity of a nation incurring debt, the more practically interesting question remains of what is to be done when the distress is past, and the country restored to a state of prosperity. Is the nation at once to strain every nerve to repay its creditors? While praising the financiers of William and Anne's reigns for their spirited policy, it must not be forgotten that when the peaceful reign of George I. dawned on a consolidated England, a small exertion would have cleared off all liabilities; in which case both the American and the French wars might

[b] The present System of Savings Banks affords an excellent proof of that possibility. Cf. Mill's "Political Economy," book v. c. 7, § 3.

[c] If we, through our contracting this loan, are able to hand down to the next generation a country well-organized, rich, and continually developing new resources, it is fair matter of calculation whether these advantages are not sufficient to counterbalance the additional burden of several hundred millions of debt. Is it better for a son to inherit from his father a healthy constitution and an encumbered patrimony, or a free patrimony and a shattered constitution?

have been defrayed by taxation (cf. ante, p. 17). An anonymous writer asserts, that an Income-tax of 12 or even 10 per cent. might have been raised during the American war; and M^c^Culloch thinks 8 or 10 per cent. would have been sufficient[d]. But these reflections are laughed to scorn by those who hold that the Debt has been a benefit, not a burden. It is necessary, therefore, to examine what Hume called "the new paradox, that public encumbrances are, of themselves, advantageous, independent of the necessity of contracting them[e]."

It seems, at first sight, the veriest paradox to say that debt, the most tyrannical of masters to the individual, can be tamed into a useful servant by the State. Yet so manifold and complicated are its effects on a country, that the assertion has great verisimilitude. When we look around us, we, no doubt, see a heavy burden of annual interest imposed on the taxes. Were the Debt abolished to-morrow, our taxes might at once be reduced to about one-half what they are at present. But we also see many advantages which the possession of a Debt seems to confer on us. It acts as a check on warlike tendencies. England, Brougham once said, is bound over to keep the peace in recognisances of 800 millions sterling. And this is the case, not only because of the actual pressure of the Debt lessening our power of sudden exertion, but because of the ramifications of our stock among other nations. We are less inclined to rush into a war with France, when we are intimately connected with her by commercial transactions. Again, it is said that this is but one of the instances in which power has passed, as in our Constitution it tends to pass, from king to people. Formerly, the king declared war on his own responsibility; now, it is virtually the people who declare war. By others, once more, the Debt is praised as being a prop to the Crown, of which, amid the present tendencies of radical philosophising, it were unwise to deprive it. And, finally, the direct benefits ascribed above to the Funding System are brought forward in support of the preservation of the Debt.

In connection with these arguments several observations suggest themselves. While it is true that the Debt is a serious burden during war, it is not the case that it acts as a deterrent upon all classes. Lord Elibanke justly observes[f], that it is the interest of the landed proprietors to avoid a war at all costs, that of the stock-jobbers to induce a war. And is there not something unworthy of a great nation in this conscious weakness, which bribes itself to keep the

[d] Edition of "Wealth of Nations," note 30. [e] "Essay on Public Credit."
[f] "Essays on the Public Debt," p. 11.

peace, fettering its quarrelsome tendencies in chains of gold? Common sense supplies us with the weightiest reasons for avoiding war: its injurious effects on commerce and industry are sufficient checks: but if an emergency arise when the national honour demands redress—and the principle of non-intervention is carried to a vicious extreme when it prevents us from most emphatically asserting that such emergencies may arise—it is mere cowardice to restrain our just indignation from fear of the burdens its expression may bring on us. In England, perhaps, at the present day, little weight need be attached to this argument for the Debt: the nation is more prone to the extreme of reticence than to that of quarrelsomeness, and stands in little need of additional inducements to prefer the former.

It is not true to say that the National Debt has shifted the responsibility of war from Crown to Commons. This, which is a favourite argument with a certain school, is quite confuted by the introductory sketch of the history of English taxation at the beginning of this essay. The whole history of our kings, from the Plantagenets to the Stuarts, is one long attempt on their part to secure to themselves the power of making war; but they never succeeded in their efforts. While the nominal right of declaring war rested, then as now, with the Crown, the power of giving practical effect to that declaration rested, then as now, with the Commons, the lawful masters of supplies. That legal right is now never sought to be over-ridden; but this result has been effected, not by the Funding System, but by the developement of public opinion and strict regard for law.

Nor is there much more truth in the assertion that the National Debt supplies a prop to the throne. At one time it might have done so. It has been already observed[6] that, had the system of loans existed at an earlier stage in our history, it might have modified the course of that history. For in those days a change of dynasty would probably have implied an abolition of debt. Had a Lancaster king borrowed from his subjects, his Yorkist successor would probably have repudiated his obligations. It was that very insecurity that made loans impossible. But circumstances have utterly changed; and it would fare ill with the Crown if its maintenance depended on props like these. A change of dynasty would not now make the slightest difference in our pecuniary relations. Even in 1688, the trifling debt bequeathed by the Stuarts was religiously respected. Possibly, had there been at that time an oppressive accumulation of debt, the result might have been otherwise. As it was, the country emphatically declared that, in expelling the Stuarts,

[6] Cf. ante, p. 9.

it was not turning over a new leaf in its history, a page on which it should begin again without reference to what had gone before, but that it was merely making a change in one detail of its organization, which did not in the least affect its position as a country. Much more would this be the case now. The Debt has developed, but so has public sentiment. Credit would hardly suffer at all, in the event of a revolution. It may be fearlessly asserted, that such an event, in the present state of the country, would not cause an alarming depreciation of Government stock. The influence of the Debt is therefore not on the side of any particular sovereign, dynasty, or party; but in favour of national stability, order, continuity, and respect to obligations.

So far the case is not a very strong one. But, it is said, however you may try to invalidate particular assertions as to the beneficial tendencies of the Debt, its general results are undeniable. A century ago, Hume and Smith predicted ruin: the debt has increased five-fold, and the country has gone on improving. So far from being a dangerous encumbrance, experience proves that the possession of debt advances the national prosperity, however that result may be reached.

Such reasoning, which Hume styled a paradox, and Hamilton disdained to answer[h], is so common now as to demand some consideration. Be it observed, therefore, that there are two sides to the question. The debt has undeniably increased; the country has undeniably improved; but such arguments as those above may be but instances of that fallacy which infers from the juxtaposition of two events their causal connection. Is it the increase of the Debt which has *caused* the increasing prosperity of the country? Or is it not simpler to explain it thus? Hume and Smith were certainly much mistaken in their estimate of the probable effects of our debt, but why? Because they did not take into account the possibility of circumstances changing. Had all things remained stationary, their predictions must have come true. Had the nation, when saddled with a debt of 800 millions, been unable to sustain a greater burden than was imposed in 1770, the Debt must have broken its back. But the prodigious improvement of the country has changed the data on which they built, and consequently invalidated their conclusions. No necessity having arisen for a repayment of capital, the only inconvenience suffered from the Debt has been an annual payment of interest. As resources increase, a larger sum can be spared annually. If a man who last year possessed £1,000 has now £10,000, he can pay ten times his former

[h] Enquiry, p. 32.

taxes without additional inconvenience. This is precisely what has happened to the country. The enthusiasm excited by the French War enabled our fathers to bear great privations, and pay a heavier taxation than had been conceived possible; and, after that war had ceased, the progress of industry soon made the Debt of 1820 weigh proportionably no heavier than that of 1770 had done. During the first few years after the introduction of railways, it is observed by Macaulay[1] that a sum exceeding the whole amount of our National Debt at the end of the American war, was voluntarily expended on viaducts, tunnels, embankments, bridges, stations, engines. The cause of all this was, not any inherent virtue in the Debt, but simply increasing prosperity.

Such is the natural explanation of the phenomena, and it disposes of all shadowy ideas of the creative power of a National Debt. Indirectly, the burden may have done good, by rousing dormant energies; but for it, our resources might not have increased as they have done. But if we seek to discover the direct grounds for a retention of the Debt, and put aside baseless theorizing and dubious advantages, we shall find it comes to be a balance of arguments pretty much as follows. On the one hand, the maintenance of a National Debt contributes to the public security. Peace abroad, order at home, are advanced by it; the latter more necessarily so. On the other hand, it adds seriously to our taxation. Its discharge would set a large amount of capital free to engage in commerce; that capital, namely, which is employed in payment of interest. Taxation may easily overstep the limit of judicious stimulation, and become oppressive. In the event of a severe war, the burden of the Debt would greatly add to the likelihood of its doing so.

The counterpoise of these two opposing considerations seems more nearly exact than has been generally supposed. The first has been unduly neglected by old writers, the second by those of our own day. But, on the whole, the balance seems to incline in favour of a considerable reduction, if not a total discharge, of the National Debt. There is little probability that the constitution of this country may soon have to encounter such a violent shock, as to make the conservative influence of a Debt necessary. That influence is but one among many, and its absence would hardly be felt. The occurrence of a revolution sufficiently strong to destroy public stability would create ruin and disaster on every hand. The National Debt is not needed to make us use every exertion to avert so frightful a calamity. And furthermore, such an event could scarcely come on us but

[1] History, chap. xix. p. 390.

after many years of difficulty, during which, and before our affairs began to be in mortal peril, there would be ample time to run up a fresh debt.

It is far more probable that this country may have to pass through a period of trial, in the course of which, though no such danger as that just mentioned may be imminent, great exertions will be demanded of it. In such a crisis, the pressure of the old Debt would assuredly be severely felt. Be it a time of war, or of social unhingement, or of commercial depression, the Debt will no longer be a harmless toy, worth keeping up for the sake of its indirect effects, but a real and oppressive incubus. Let not the lesson of the great French war be thrown away. Let us make our preparations while we can. If it be thought that the entire discharge of the Debt would cause unnecessary distress by destruction of investments and so forth, at least a large reduction might be made without much inconvenience. If we reduce the Debt by half, we shall annihilate one fifth of the expenses which, under present circumstances, must be annually met at whatever cost.

What disadvantages would ensue from paying off the Debt? The grand objection seems to be that we should have more money than we knew what to do with! It is difficult to conceive that some remedy will not be found to avert any bad consequences which may result from such a plethora of wealth. Any great reduction must be effected gradually. If this be properly managed, if the markets have time to get habituated to each new change, there is no reason to doubt but that industry will expand to receive the new capital. English commerce, it may fearlessly be said, has room for it all and to spare. We shall thereafter be enabled to reduce our taxation by a far swifter method than at present. Many luxuries, which have now well-nigh become necessaries, are still rated at an absurdly high duty[k]. Progress of all kinds would advance more rapidly; for high taxation, and the consequent high price at which the means of life are sold, never fail to cramp a nation in its onward path. Surely such an experiment is worth the trying. We have seen, we are now seeing, a great example in our own times of what a mighty country can do when it sets its shoulder to the wheel. In the late American Civil War, a Debt was run up from little or nothing to well-nigh six hundred millions in the course of four years. Statesmen stood aghast at this precipitous rush down the steep places

[k] Unless, indeed, we believe with M^cCulloch ("Circumstances which determine the Rate of Wages," p. 97), that high taxes on spirits and tobacco are laudable, since they act as sumptuary penalties on indulgence! The duty on American Cavendish tobacco at present quadruples its price.

of debt, and predicted national bankruptcy and shame. But, the contest over, the States addressed themselves in strong earnest to the work of reduction; and, not by a succession of strains and slackenings, but by one steady though rapid progression, they are fast reducing their gigantic burden to manageable compass. We may not have the resources of that wonderful country, but we have enough for our own necessities. Let history, let precept, let example teach us; or we may have to learn the lesson after rougher fashion, in some darker hour.

Since, then, it seems desirable that the National Debt should be reduced, the question arises what is the best means of doing so? An examination into this point will conclude this essay, and will embrace a more detailed, though necessarily brief, inquiry into the nature of those Sinking Funds and other appliances, which were mentioned as brought forward at different times by different statesmen.

The most obvious plan for reducing the pressure of a National Debt is by lowering, as far as possible, the interest paid on Government Stock. When we remember that 10 per cent. was offered on the first loan contracted by Government—the cause of this apparent munificence being partly the high rate of interest then common, and partly a want of confidence in the security—it will naturally be expected that, as these causes ceased to operate, Government would take advantage of the change of affairs to procure easier terms. And this was done: but not without much opposition, at long intervals, and accompanied by extravagance which largely neutralized its beneficial effects. We have already seen how Walpole opposed the reduction of interest in 1737, and procured the rejection of Sir John Barnard's bill. Before this, however, the rate of interest had been brought down in 1716 to 5 per cent. on most of the funds; in 1727 a further reduction to 4 per cent. was effected; and in 1749 Pelham and Barnard succeeded in carrying the measure which Walpole had opposed. By this act the larger part of the Debt was reduced to 3 per cent. But there still remained a considerable portion funded in other stocks; and it was not until 1854 that the last of these was reduced to 3 per cent.[1]

The full advantage of these reductions, however, was for long denied us, owing to the suicidal practice affected by Government of funding by increase of capital, to avoid a temporary rise of interest. In order to preserve a nominal

[1] A full account of these various stocks, from 1820 to 1855, will be found in the Parliamentary Return, August 10, 1855, (Accounts and Papers, vol. xxx. p. 253).

interest of 3 per cent., it was the almost invariable practice to grant a larger stock than that ostensibly purchased [m]. Government is necessarily obliged to buy high and sell cheap: for in time of war, when its debts are contracted, the value of stock is diminished, and when in time of peace it buys up the stock thus created, its value has risen. In point of fact, it may be said to buy at £60 and sell at £80. It would have been far better to have bought and sold at par, and faced the temporary increase of interest [n]. In the earlier years of the Funding System this wise plan seems to have been followed: but in each year of the Seven Years' War the stock created was in excess of the money actually received, and from the beginning of the war with America to the end of that with France this objectionable practice was recklessly carried out. As the three per cents. had occasionally fallen to little more than half their nominal value, it follows that in paying back those loans we should have to pay £100 where we received between £50 and £60: and so in proportion with the other loans. Some instances of this are given by M^c^Culloch ("Taxation and Funding," p. 440 seq.): and the same writer estimates the *annual* loss caused by this creation of artificial stock, through all those long years, at from 6 to 7 millions (p. 449).

This system has been long abandoned, and will scarcely be revived. But we can hardly look for any further reduction of interest for some time to come. In these days of large profits, 3 per cent. is perhaps the most moderate interest our Government can offer: any attempt at diminution would excite general discontent, and probably prove impracticable. For Government can only procure a lowering of interest by offering to buy up those who decline to accept the reduction [o]: and, should the body of recalcitrants be numerous, it may be doubted whether Government could meet this obligation. We must therefore look elsewhere for our means of reduction.

A passing notice may be given to the proposal to reduce the Debt by purchase of the land-tax. This tax having been in 1798 rendered permanent at a fixed rate, it was possible to calculate the charge on each estate. The owner

[m] Hamilton's "Enquiry," part iii. chap. vi.

[n] If it be true, as has been asserted, that an increase of interest from 3 to 3½ would have sufficed without increase of capital through the whole French War, it is difficult to regret in strong enough terms the blindness of our financiers.

[o] This supplies an answer to Ricardo's defence of this system. He asserts (Works, p. 538) that people would not have invested at high interest, because they must have known it would be lowered at the first opportunity. But they were always given the choice of accepting the lowered interest, *or receiving back their loan.*

was then permitted to buy off this tax by purchasing capital in the 3 per cents. to an equivalent amount. This scheme was coldly received, only one-third of the land-tax being thus redeemed by 1817; and the result is not surprising. The landholder, in paying all at once, has not received any advantage in the way of easier terms: the burden has merely been thrown on one year, instead of being distributed over many. It would be just as reasonable for any private individual, who was liable to some annual charge, to invest a sum in stock, whose dividend should meet this annual charge. No more rational ideal of pecuniary management can be imagined; but unfortunately it is not always possible. Most men, even if they be landholders, have quite enough to do to meet the charges of the current year.

We come now to examine the rationale and practical working of the celebrated Sinking Fund. The history of this fund affords a striking example of the extent to which men's judgment may be misled by their wishes, and ought to prevent our lending too easy credence to any views on this subject, however generally adopted. When temporary taxes, proving insufficient, were renewed, and finally made permanent, it became apparent that great difficulty would be experienced in paying off the debt. When, in 1716, the various loans were amalgamated, and all the revenue, except that portion devoted to "Civil Expenses" (as the cost of carrying on Government was then styled), assigned to paying the interest of the Debt, there being a considerable surplus, it was natural to set this apart for repayment of capital. The question then arose, how this could best be done. Was there no possibility of improving on the slow process of paying a small portion of the debt with each year's surplus? Would it not be better to mass these surpluses, year by year, into a fund, whose interest should be added to it each year, until it reached a considerable sum? Earl Stanhope was the first to answer this question in the affirmative, his scheme, from the ministry under which it was brought forward, being usually known as Sir Robert Walpole's. So far there was little harm in the measure. But, in addition, it was enacted that even when there was no surplus, the same yearly sum must be paid into the fund. The effect of this was, that in each year when there was no surplus, we had to borrow in order to pay this yearly sum. Thus, though at first some portion of the debt was paid off, as soon as war broke out, the Fund became nugatory. Between 1718 and 1732 about $6\frac{1}{2}$ millions of old debt were paid off, and about 8 millions of fresh debt contracted.

The advocates of the Sinking Fund, however, did not

think it had had a fair trial, as it had been very soon broken in on and mortgaged by anticipation. Accordingly, in 1774, Dr. Price published his famous "Appeal to the Public on the Subject of the National Debt," which gave rise to the measures adopted by Pitt, and afterwards by Petty and Vansittart. This writer pointed out—and his assertion is said to be mathematically correct—that a penny, put out 1800 years ago at 5 per cent. compound interest, would by this time have reached a sum equal to 150 millions of globes of solid gold, each the size of our earth[p]! Therefore, he argued, all we have to do is to set aside any sum we can conveniently spare, and let it mount up at compound interest till it equals the National Debt, to whatever sum that may then have reached[q]. The nation adopted this belief; with what results we have already seen.

Without entering into the details of Pitt's three plans, is it possible to detect the fallacy which is now generally acknowledged to have warped his judgment and those of his successors? It may be put popularly thus:—they had not taken into account who was to pay the interest. It is perfectly true that a million, put out at 4 per cent. compound interest, will, in 105 years, reach 1,575 millions—but how is the result effected? It is by the banker paying each year an increasing sum as interest on the increasing capital; and, in the case of a Government loan, on whom will this burden fall but on Government? In the case of Price's millions of globes, in order to reach the splendid total promised, we shall have had to *pay* several millions of globes by way of interest!

This will be made clearer by examining the practical working of the Fund at a time when there is no surplus. The Government is burdened with some heavy expenses, to meet which it calls for a loan. Besides these special expenses, there are the ordinary outlays still necessary, and one of these is the yearly payment to the Sinking Fund. The loan has simply to be made large enough to include this as well as the other expenses. Thus, in order to keep up the Fund for paying back our Debt, we are obliged to contract new debts. It will be seen that this is really a piece of "jugglery:" we *re-arrange* our Debt, and—hey, presto!

[p] For other "paradoxical effects ascribed to the increase of money by compound interest," see Hamilton, Note IV. In a certain M. Ricard's will it is estimated that 100 livres may, at the end of five centuries, have been increased to four millions of millions of livres.

[q] "Appeal," p. 326 in Overstone's reprint; the calculation may be found in his "Treatise on Reversionary Payments," Introd., p. 13. Many of his statements originally appeared in this volume (chap. iii). It should be said, that another calculation makes the number 107 millions in 1,773 years, and that the interest calculated was 5 and a fraction.

we are told that part has disappeared in the transposition. Yet this is, in sober earnest, what for long was believed by our best statesmen. The Sinking Fund was believed to increase, without costing anyone anything[r].

These remarks only apply to a time when the expenditure is in excess of the taxation. At other times a Sinking Fund can do little harm. But it must be remembered that the magical effects of compound interest are enormously thrown back by any temporary interruption. Therefore it was the very essence of Price's scheme to prevent such interruptions. He even asserted that the Fund was never so beneficial as during war, and that to suspend it then was the "madness of giving it a mortal stab at the very time it was making the quickest progress towards the accomplishment of its end." It is better to borrow fresh loans; for we thus borrow at simple interest to improve it at compound.

These extraordinary assertions have been just answered by shewing the practical working of the Sinking Fund during war. The theoretical answer is, that the Fund does *not*, as is asserted, increase at compound interest. This can only be the case when capital is employed in some sort of productive industry. When the Commissioners for the Fund buy one million's worth of stock, they will next year receive the dividend on it. Suppose they purchase additional stock with this dividend, they will certainly receive a larger dividend next year; and so on increasingly. But this dividend is paid from the produce of taxation; and, as the dividend increases, a larger proportion of the taxes has to be set aside to pay that dividend. The sums thus applied would otherwise have been remitted to those taxed. The delusion is now apparent. Were there a certain amount of capital employed in some industry, and the profits each year added to the principal, the capital would certainly increase after the fashion Price described. But in his Fund, so far from its being independent of the taxes, the sole means of support was the produce of taxation, or a fresh loan.

Thus the Sinking Fund, as understood by financiers during the French war, is a mere bubble. When there is a surplus, it certainly reduces the Debt; but how? Merely because the heavy taxes, imposed during times of greater distress, are continued instead of being remitted. Precisely the same result would be achieved without the Fund, were the taxes kept at the same height: except, indeed, that we

[r] "It was owing to the institution of the Sinking Fund that the country was not charged with a much larger amount of debt. *It was an advantage gained by nothing*, and a system likely to be attended with still greater advantages."—*Lord Henry Petty's Budget-Speech, March* 29, 1806 (*quoted by Hamilton.*)

should save the Commissioners' expenses. And when there is no surplus, the preservation of the Fund is a mockery. We simply borrow in one place to pay in another. Not unfrequently it is worse than nugatory. This process of transference is not unfrequently attended with loss, besides that it involves paying Commissioners. It has again and again been the case that the Commissioners have had to pay higher interest on their fresh loan than they were receiving on their Fund; and in this case the difference was, of course, as completely sacrificed as if it had been thrown into the sea.

It would be easy to enter into fresh particulars; but perhaps the above details and arguments may be sufficient to shew the inutility of the Sinking Fund, which, soon after the publication of Hamilton's book, was quietly shelved by Government. Before leaving the subject, therefore, let us merely glance at one or two points which have been urged, not in defence, but in palliation, of the Sinking Fund system. It is said that it kept up the public confidence. Granting such a pious plot were justifiable, why not, as Grenfell proposed [s], let the Commissioners, instead of borrowing elsewhere, subscribe the amount received by them to the various loans? This would have avoided all the expenses of transference. Again, it is said, that were the taxation sufficient to pay, not only the interest on any particular loan, but also 1 per cent. on the stock so created, a Sinking Fund of this kind would not take long to repay that loan. And this is undeniable; but the result is due, not to any virtue of the Fund, but simply to the heavy taxation [t]. Finally, it is said that the Sinking Fund supports the price of stock. It may be answered, that this support takes effect at the very time when it is of consequence to obtain stock low. It seems also, however, very dubious whether this result is really produced. It is true that, at a time when stock is falling, Government steps in as a purchaser on a large scale; but it is no less true that this interference obliges it to ask for an additional loan, and this is surely tantamount to neutralising the good effect its interference produced. If, however, this calculation be mistaken, and if, circumstances remaining the same—which is a dangerous assumption to make in a continually advancing country—the price of the 3 per cents. could for some time be kept above par by means of the Sinking Fund, it is possible that a further reduction of interest might be effected on the Debt.

[s] M^cCulloch, "Taxation and Funding," p. 460. Grenfell's proposal is defended by Ricardo, Works, p. 529.

[t] This is precisely what was done by the Sinking Fund in any year when there was a surplus. Cf. last page, and remarks there. (It may be mentioned that this was Pitt's original scheme, though it was soon broken in on.)

We may now take leave of the Sinking Fund, once so enthusiastically upheld by high and low—"that sacred blessing; the nation's only hope[u]"—but now scarcely known by name to any but students of Political Economy. It is scarcely probable that, for the sake of the very problematical advantage hinted at just above, it will ever be rescued from the well-merited obscurity to which it was consigned by Act 10 Geo. IV., cap. 27[x].

The last proposal to which our attention must be turned is that which aims at paying off the National Debt by some sort of assessment on capital. This is an intelligible enough scheme, and has occasionally met with supporters. It was advanced, during the reign of George I., by Archibald Hutcheson, a staunch opponent of the Funding System. It was again advanced by the Whig party shortly before the Reform Bill of 1832, and stoutly resisted by Tory Organs[y]: and it may reckon among its adherents the great name of Ricardo[z]. Nor is it devoid of a certain captivating plausibility. Seeing that in reality each individual in the nation owes a part of the Debt, why should we not all make an effort and pay up our shares, the proportion each individual has to contribute being determined by the property he possesses? We may go the length of saying that, if this scheme were feasible, it would be the fairest possible way of paying the Debt. But it would be impossible to carry it out with justice, or perhaps even at all. In the first place the nation, not feeling any particular evil effects at present from the Debt, would strenuously oppose any plan of reduction which did make itself burdensome. In the second place, such results could not fail to follow from this plan. The difficulty which Hume suggested, in reference to Hutcheson's scheme, is still unanswered: viz., the impossibility of getting the stock-holders to pay their fair proportion, or the poor to pay at all. Ricardo suggests that there would be a plethora of money among the paid-off stock-holders sufficient to meet the corresponding demand on the part of the land-owners, and that therefore they may be left to make their arrangements with each other.

[u] Price's "Appeal," p. 338.

[x] "Of course we need not go back to any question of a sinking fund. A sinking fund is an exploded idea."—*Mr. Lowe's Budget-Speech, April* 11, 1870. (Yet the explosion had not taken place fifteen years ago, when, a loan of 16 millions having been imposed to meet our expenses in the Russian war, it was enacted that, after the close of the war, one million should be paid annually to the Sinking Fund, until by this means 11 millions of our funded debt had been discharged).

[y] Cf. "Edinburgh Review," vol. xlvi. p. 407; "Blackwood's Magazine," vol. xxiii. p. 345.

[z] This was the logical issue of his uncompromising hostility to the Funding System.

They might settle it "by loan, or by sale and purchase, as they might think it most conducive to their respective interests; with this the state would have nothing to do [a]. The question as to the poor he does not touch. The Edinburgh Reviewer takes much the same ground, but is still less inclined to favour the land-owners. Admitting that the poor could not pay their share, he thinks it should be done for them by their masters, who would ultimately reap the benefit, since the great consequent decrease in taxation would bring about a corresponding decrease of wages. Owners of land must be left to take their chance: the probability is that they will have to pay more than their due quota, but that cannot be helped [b]. It is evident that Hume's objection has not been met, and it cannot be thus disposed of with a high hand. Without stigmatizing such an assessment of capital, with the writer in Blackwood, as unparalleled robbery [c], it is manifest that it would entail a large amount of the grossest injustice.

In truth, the unanswerable objection to any such scheme is its utter impracticability. The attempt to enforce it would almost certainly end in a revolution. The utmost that can be said for it is that, in the event of a sudden and enormous reduction of the National Debt becoming necessary—a contingency which is not even remotely probable—such an attempt might be preferable to bankruptcy. It might be possible, with a vast amount of oppression and misery, to pay off one half the Debt by this means, though it might not improbably draw on the bankruptcy which we should be trying to avoid, and which would be but a shade worse than this remedy: but until that contingency arrive, it would be madness to seek to cure an evil whose effects are little felt at present, by one which would shake the country to its lowest foundations.

We set out with the understanding that a reduction of the National Debt was desirable. After examining those fair schemes which promised so much, and by which so little has been effected, we find ourselves unable to regard any of them as worthy of adoption. What course, then, is left? None but the simple plan of devotion of surplus. "The excess of revenue above expenditure," in the words of one of Hamilton's General Principles, "is the only real sinking fund by which the public debt can be discharged." To this conclusion all our enquiries have brought us. And but one

[a] Works, p. 545.

[b] "Edinburgh Review," vol. xlvi. pp. 409, 410.

[c] "Never, not even in the worst periods of Rome, did the heads of her factions, in all their auctions of rapine, set up to sale the goods of the conquered citizens to such an enormous amount."—*Blackwood's Magazine*, vol. xxiii. p. 346.